

August 27, 2013

How to Measure the Success of Your Compensation Strategy



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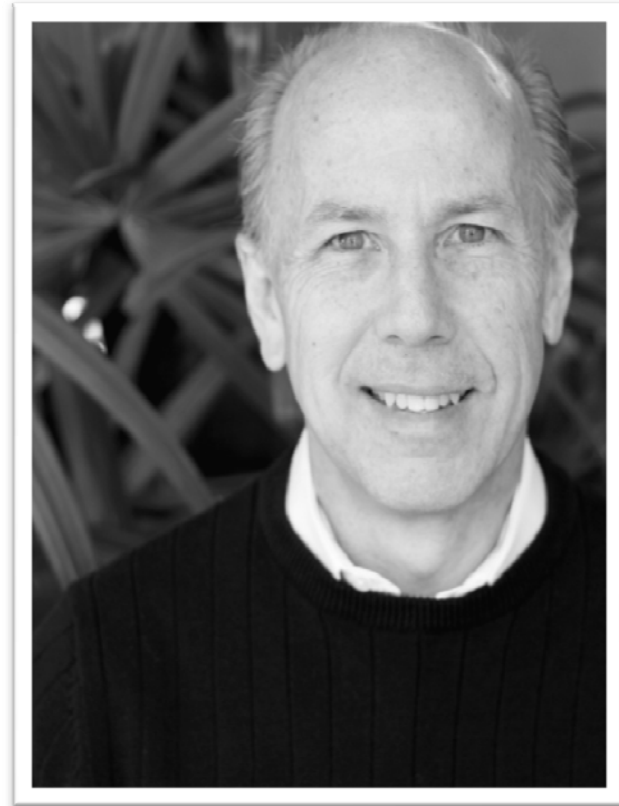
Today's Presenter:

Ken Gibson

Senior Vice President

(949) 265-5703

kgibson@vladvisors.com



7700 Irvine Center Drive ♦ Suite 930 ♦ Irvine, CA 92618 ♦ 949-852-2288

www.VLadvisors.com ♦ www.PhantomStockOnline.com



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Today's Presenter:

Joe Miller

Senior Consultant

(949) 265-5708


jmiller@vladvisors.com




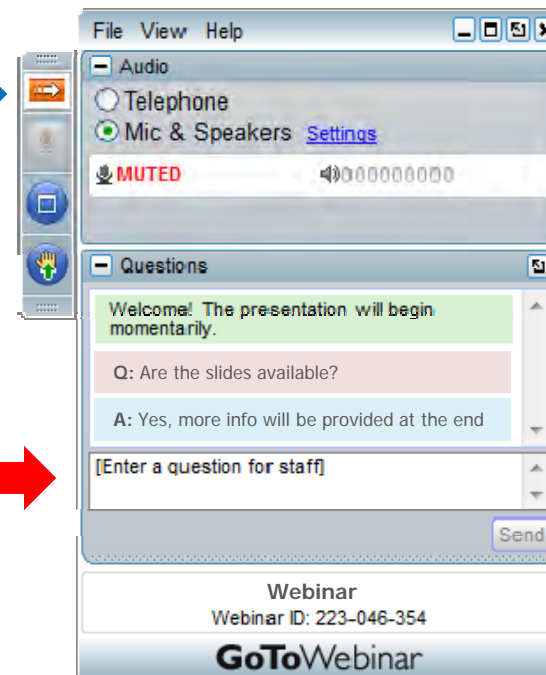
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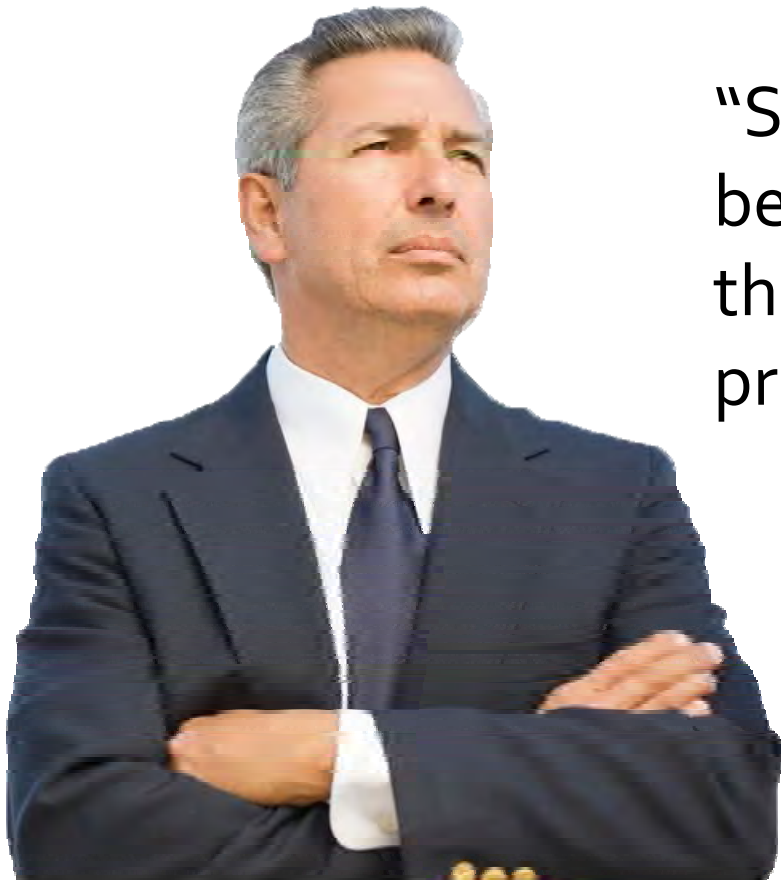
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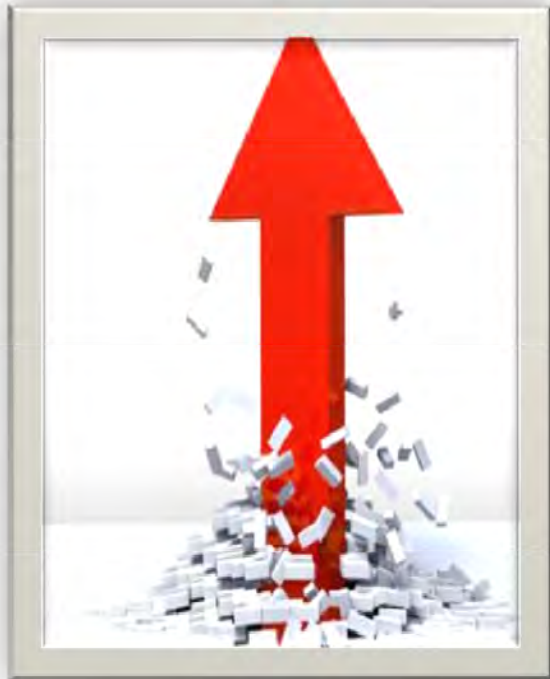
Common Question

Potential Client

“So...what results have your clients been getting since you’ve helped them with their compensation programs?”



Right Idea, Wrong Question



Scenario:

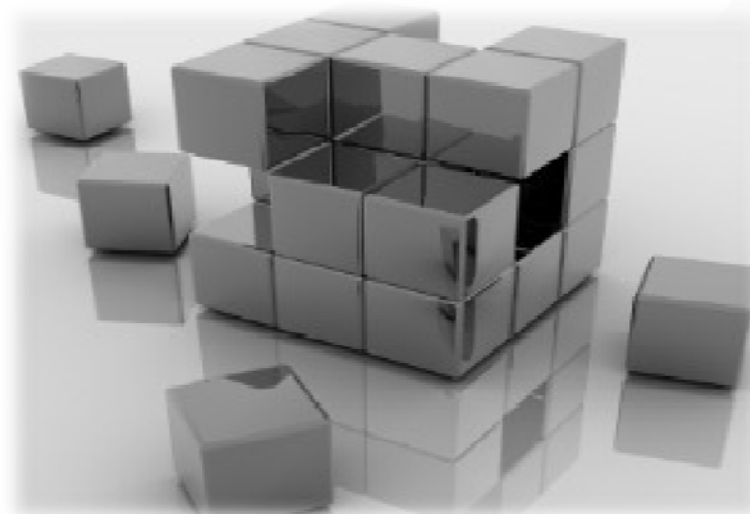
- Company installs a phantom stock plan
- Goes on to double revenues in the next three years

Questions:

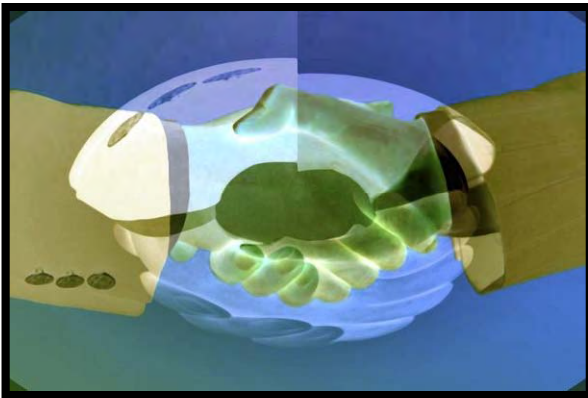
- Is that success attributable to the phantom stock plan?
- What if revenues had gone down? Is the phantom stock plan to blame?

Potential Factors

- New Product Introduction
- Key acquisition
- Competitor leaves the marketplace
- Caught some phenomenon in the economy at just the right time
- Etc.



So...What Role did the Phantom Stock Plan Play?

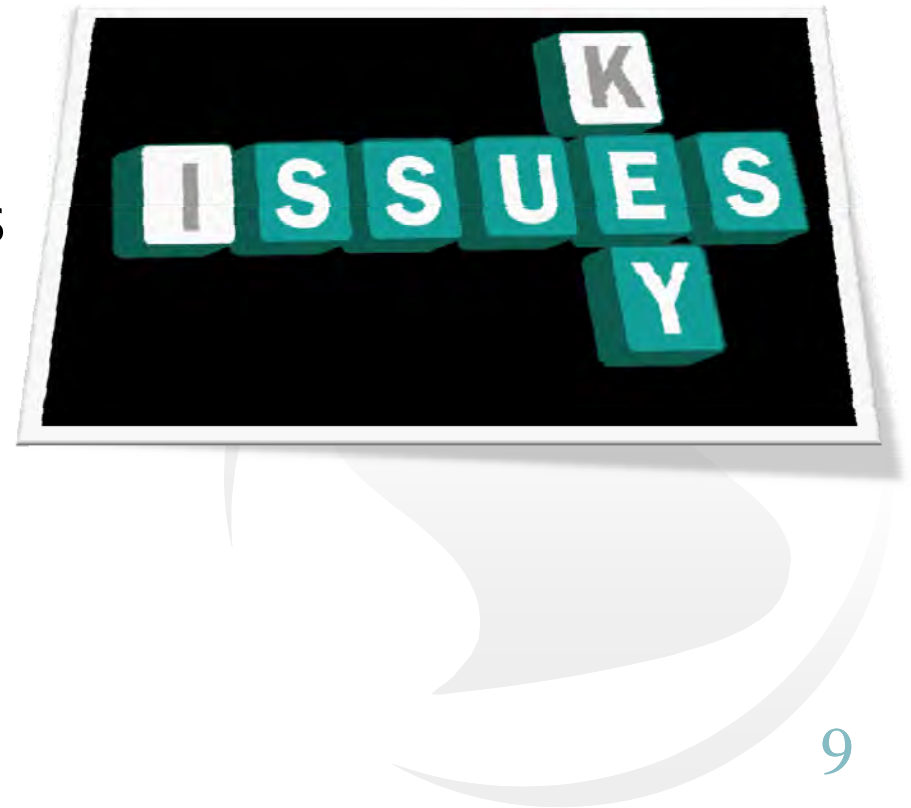


- Provided definition of value creation for business
- Established how value would be shared
- Defined a financial partnership with key producers
- Increased the attraction and retention of premier talent (who drive results)
- Provided a channel for fulfilling compensation philosophy

The Right Questions

How do you define
“Success”?

- What is the role of a compensation plan?
- How do you determine if it's fulfilling that role?
- How do you ensure it is successful in its role?



The Key to Success—Starting Point

Form a Total Compensation Structure



Total Compensation Structure

- Meaning
- Types
- Benefits
- Construction



Building the Structure

Steps

- Establish a Pay Philosophy
 - Supportive of business growth plan
- Assess current practices and plans
 - Structure
 - Mindset
- Develop a Compensation GamePlan
 - Compatible with business vision, model and strategy
- Design and test rewards elements
 - Salary Ranges, Incentives, Core Benefits, Retirement Programs
- Implement a rewards management system
 - Launch strategy
 - Communications plan
 - Financial and statutory oversight
 - Plan administration
 - Strategy assessment and adjustment



Compensation Philosophy



- Does the company have a written compensation philosophy statement?
- Does it clearly articulate what the company will pay for and how it plans to share value?
- Does it define where the company wants to be relative to market pay standards for salaries and total compensation?
- Does it establish a balance between guaranteed and incentive pay?
- What about between short-term and long-term incentives (or what VisionLink refers to as value-sharing)?

Know Your Philosophy (Sample Statement)

- We believe in paying base salaries at the 40-50th percentile but in providing unlimited upside earnings through value sharing
- We believe value should be shared with those who help create it – Pay for Performance
- We believe value sharing should be split 50/50 in rewarding short-term and long-term performance



Assess Current Practices and Plans

- Market Pay Assessment

Compensation GamePlan (Sample Recommendations)

- Realign salary ranges to market (40-50th Percentile)
- Redefine bonus targets (market median)
- Develop a Long-Term Incentive Plan
 - Not interested in sharing actual equity
 - Ideal plan shares a percentage of growth with top management
- No changes to core benefits or retirement



Building a structure - Where do you start?

- Typical structure development starts with salaries
- Four Approaches
 - Pure Market Pricing
 - Traditional Grade Structure
 - Broadband Structure
 - Hybrid Structure



Pure Market Pricing Approach

Creates a fixed range of pay for positions based exclusively on market data. Rewards eligibility and targets are set at the position level.

Role	Market Source	Salary		
		25th	Median	75th
Accountant I	Towers Watson - Accountant I	38.1	42.1	43.2
	Mercer - Accountant Level I	35.5	37.4	39.8
	Pearl Meyer - Junior Accountant	40.1	44.2	47.4
	Radford - Accountant Entry	37.6	39.1	43.1
	Average	37.8	40.7	43.4

Role	Market Source	Salary		
		25th	Median	75th
Accountant II	Towers Watson - Accountant II	46.3	51.1	52.5
	Mercer - Accountant Level II	43.1	45.4	48.3
	Pearl Meyer - Accountant	48.7	53.7	57.6
	Radford - Accountant Intermediate	45.7	47.5	52.4
	Average	45.9	49.4	52.7

Role	Market Source	Salary		
		25th	Median	75th
Accountant Senior	Towers Watson - Accountant III	54.8	60.6	62.2
	Mercer - Accountant Senior	51.1	53.8	57.3
	Pearl Meyer - Accountant Senior	57.7	63.6	68.2
	Radford - Senior Accountant	54.1	56.3	62.0
	Average	54.4	58.6	62.4

Pros:

Highly accurate. Works well in very small companies where positions are common.

Cons:

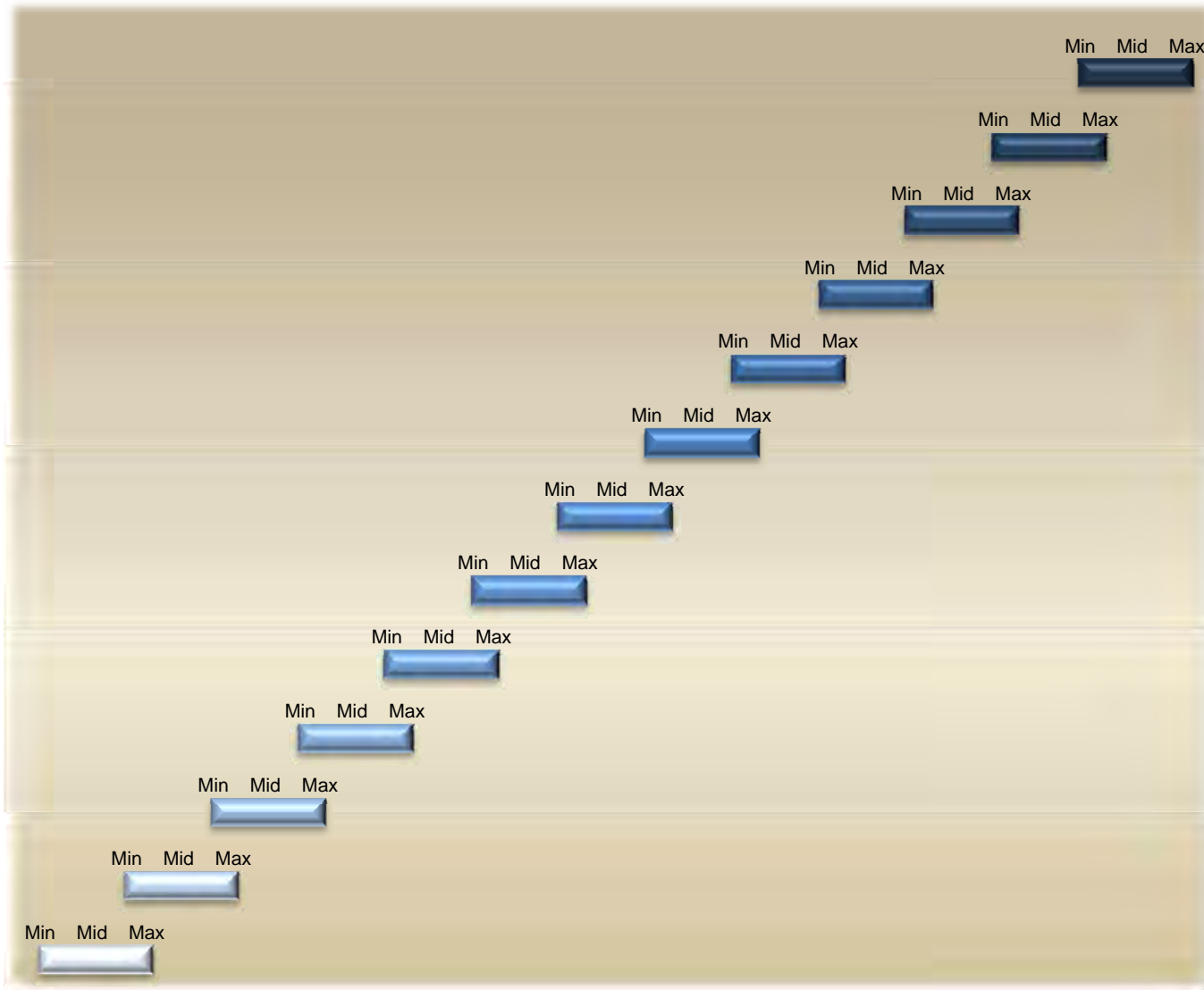
Can be administratively burdensome. Lack of relevant market data for positions makes it challenging to establish a pay range.

Example Use:

A small hierarchical accounting firm with very limited rewards structure.

Traditional Salary Structure

Positions are categorized inside of a system with many ranges, each with a minimum midpoint, and maximum. Rewards eligibility and targets are determined by level.



Pros:

Provides narrow ranges of pay for all positions. Works well in very large, highly structured promotion minded organizations i.e.: Government, Military, Universities.

Cons:

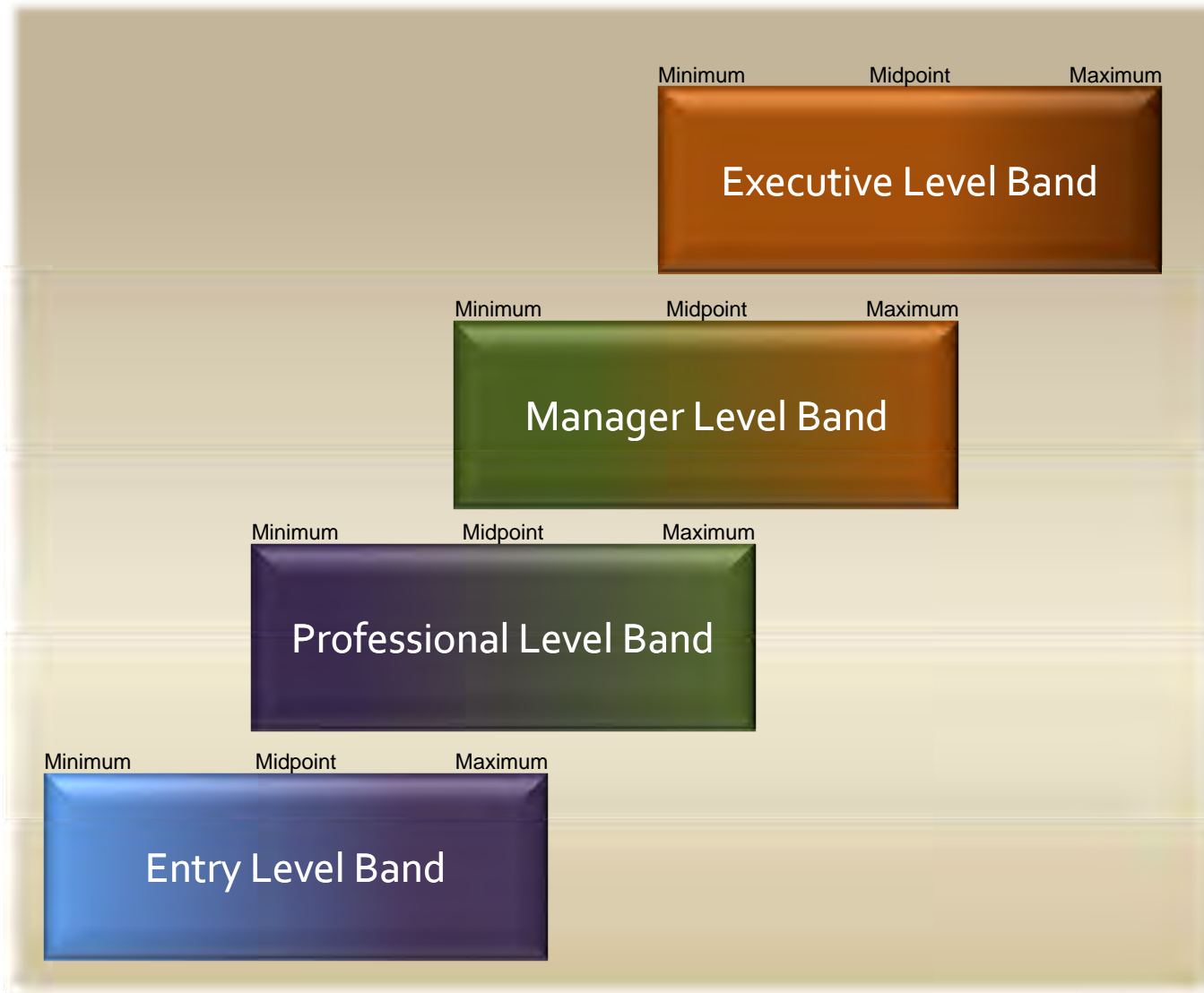
Extremely Rigid. Very little overlap of ranges. Can be difficult to maintain and administer.

Example Use:

The U.S. Military, where promotion into a new position may grant you access to a new level of reward eligibility

Broadband Structure

Positions are categorized inside a few broad ranges to allow for maximum discretion in pay decisions. Rewards eligibility is flexibly determined by band.



Pros:

Provides maximum flexibility for making pay decisions.
Simple to administer.
Focuses on lateral movement rather than promotion.

Cons:

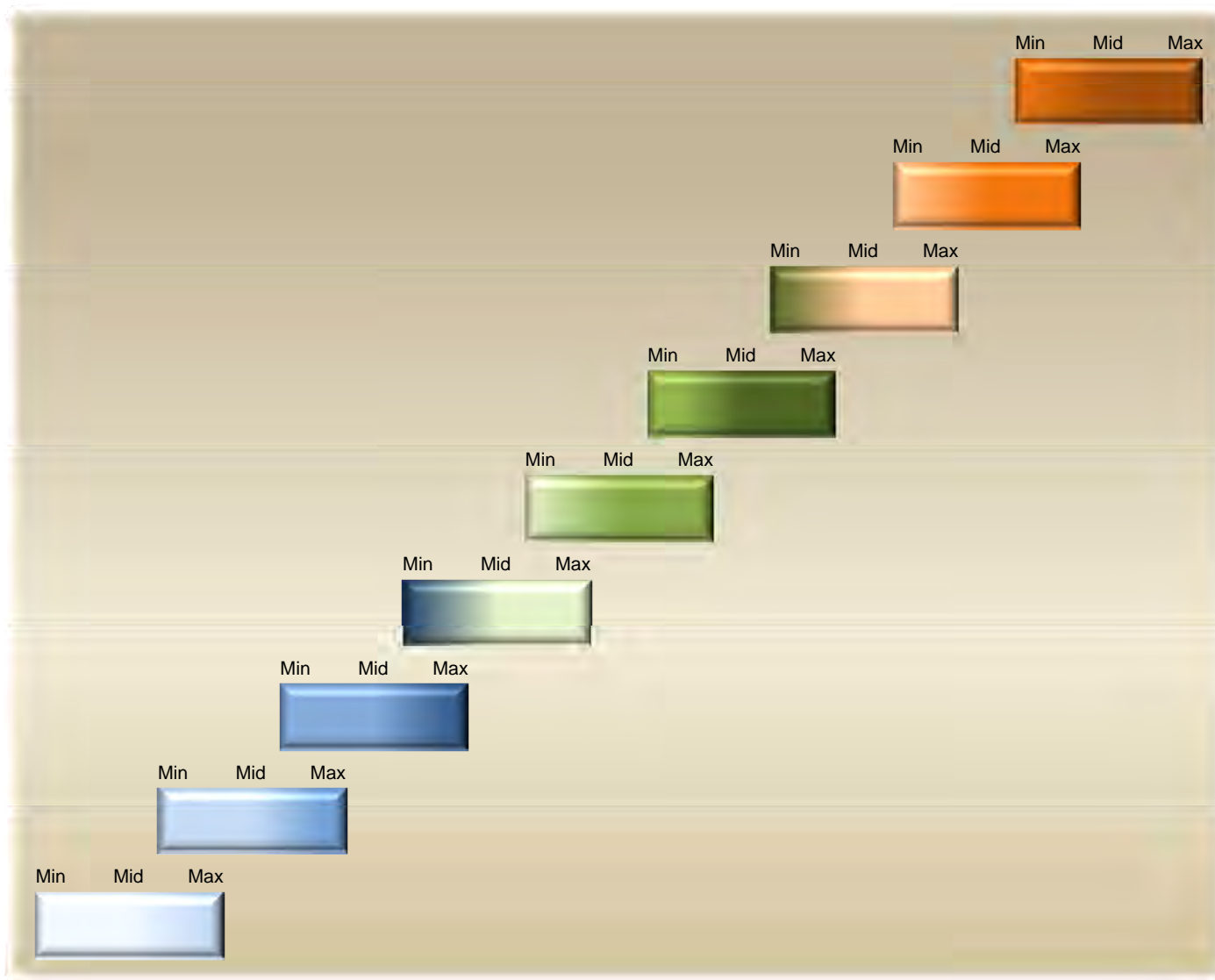
May not provide tight correlation to actual market conditions. Actual pay, although inside the range, may not be tightly correlated to the market.

Example Use:

A progressive online business where employees are encouraged to explore lateral moves over promotion. High level of rewards flexibility and eligibility is simply defined.

Hybrid Rewards Structure

Allows for broad flexibility inside of a progressive pay hierarchy.



Pros:

Combines the best of elements of a broadband and traditional structure.

Cons:

Does not capture the full value of either a broadband or traditional structure.

Example Use:

Hybrid structures are fairly common today. Because of the number of bands/grades it is easy to tie eligibility to multiple rewards programs. They support both lateral movement inside the grade as well as promotional movement to the next grade.

The Final Structure

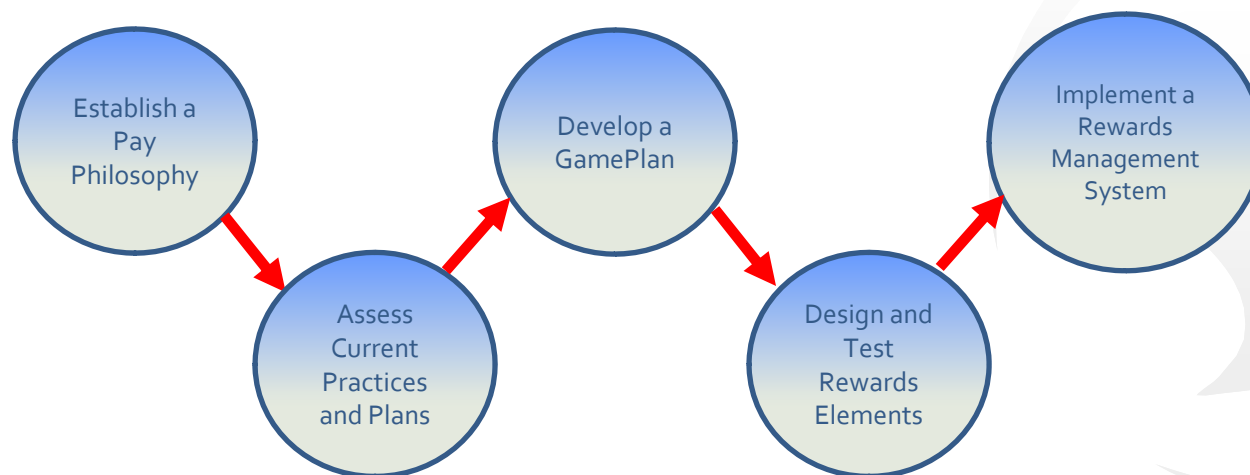
Grade/ Band	Salary Range			Bonus Target	LTIP Target	% Phantom Stock FV	% Phantom Stock AO	401k Match Max %	Deferred Comp Eligible	Deferred Comp Max Match	Health, Dental, Life	Vacation Days	Sick Days	Financial Planning Perk	Annual Car Allow
	Min	Mid	Max												
1	203,531	271,375	339,219	50.0%	100%	50%	50%	5%	Yes	5%	\$11,141	Unlimited	Unlimited	15,000	20,000
2	150,078	200,103	250,129	35.0%	75%	50%	50%	5%	Yes	5%	\$11,141	Unlimited	Unlimited	10,000	12,500
3	119,497	159,329	199,161	25.0%	50%	100%	0%	5%	Yes	5%	\$11,141	25	5	5,000	8,000
4	102,632	136,843	171,054	20.0%	25%	100%	0%	5%			\$6,127	25	5	5,000	
5	81,293	101,616	121,940	15.0%				5%			\$6,127	25	5	5,000	
6	69,720	87,150	104,580	15.0%				5%			\$6,127	15	5		
7	58,564	73,205	87,846	10.0%				5%			\$6,127	15	5		
8	50,176	62,720	75,264	10.0%				5%			\$6,127	15	5		
9	44,038	51,809	59,580	5.0%				5%			\$6,127	15	5		
10	37,211	43,777	50,344	5.0%				5%			\$6,127	10	5		
11	30,784	36,217	41,649	5.0%				5%			\$6,127	10	5		
12	23,562	27,720	31,878	5.0%				5%			\$6,127	10	5		
13	19,529	22,975	26,421	0.0%				5%			\$6,127	10	5		
14	17,354	20,417	23,479	0.0%				5%			\$6,127	10	5		



Manage the Process

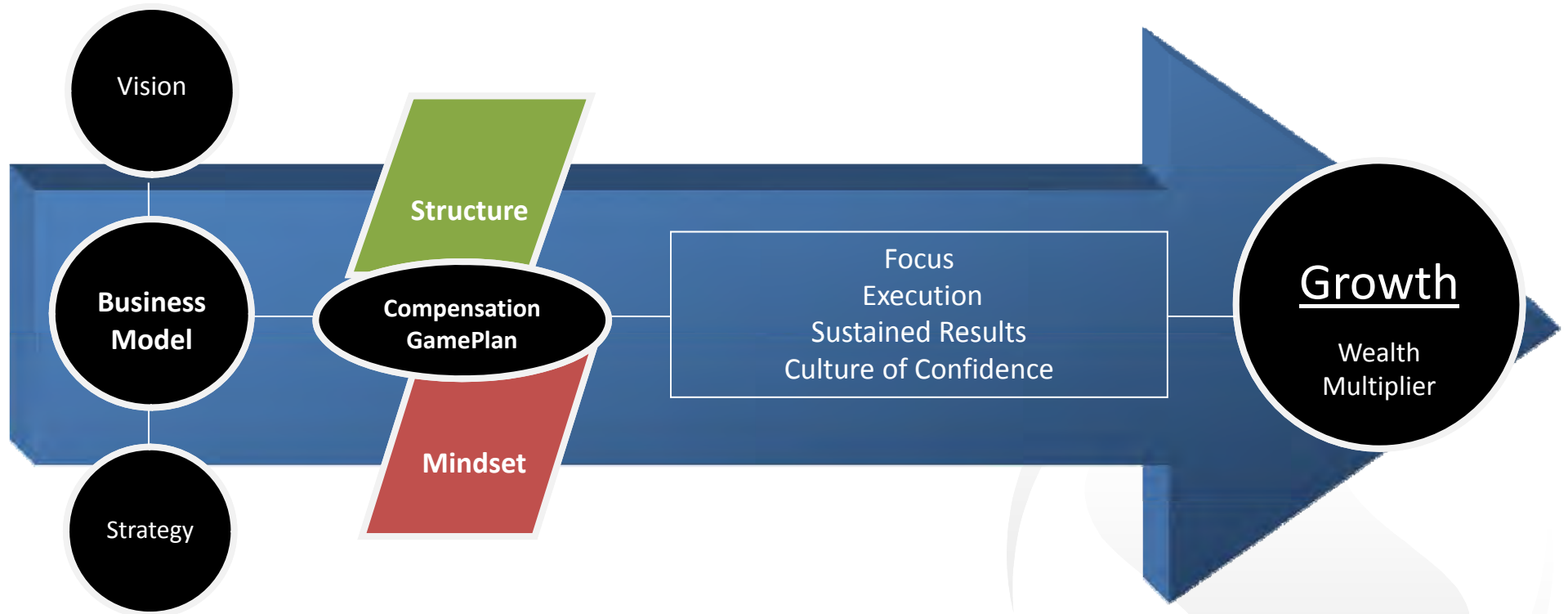
- Launch the structure/implement the change
- Communications plan
- Financial and statutory oversight
- Plan administration

★ Strategy assessment and adjustment ★

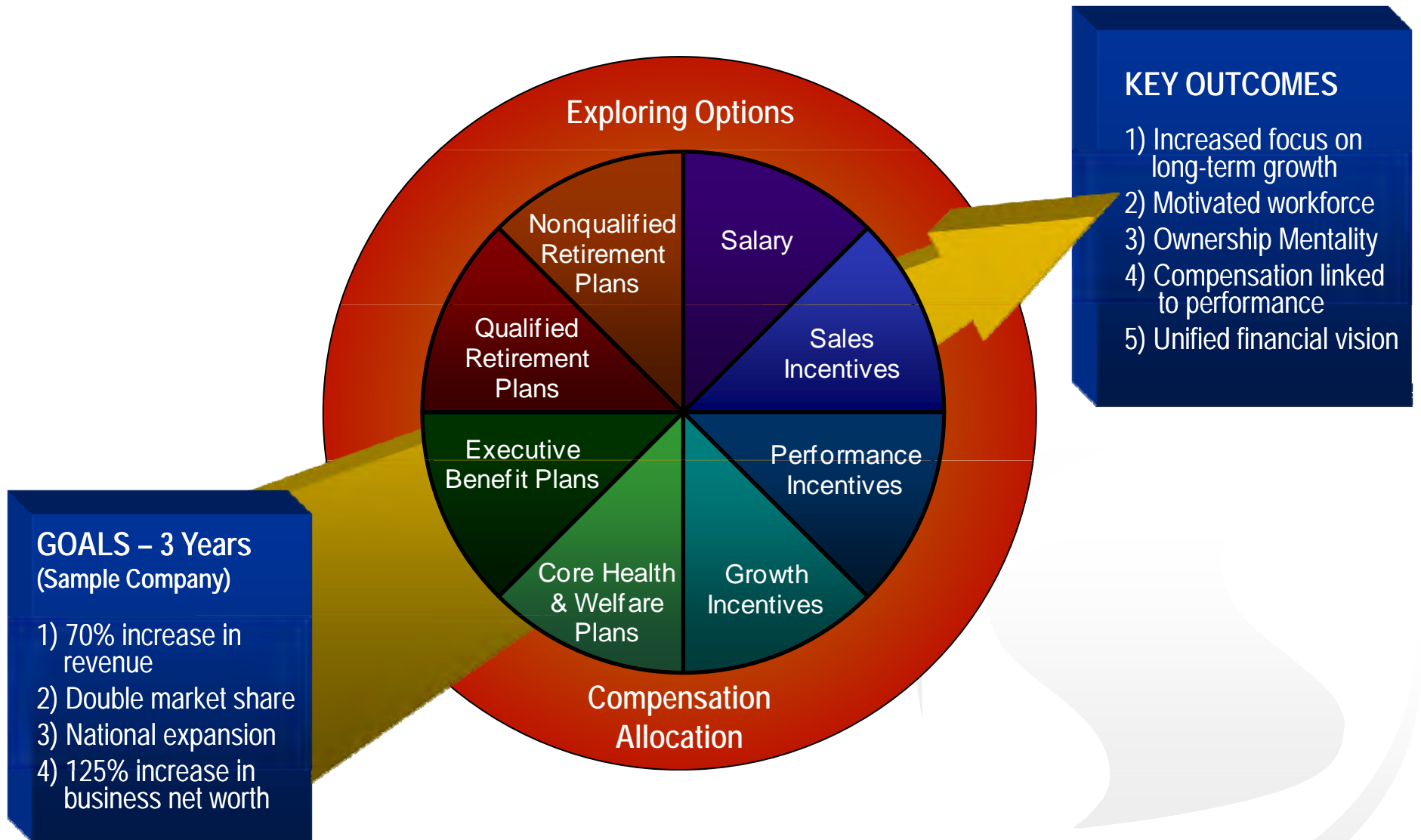


Framework:

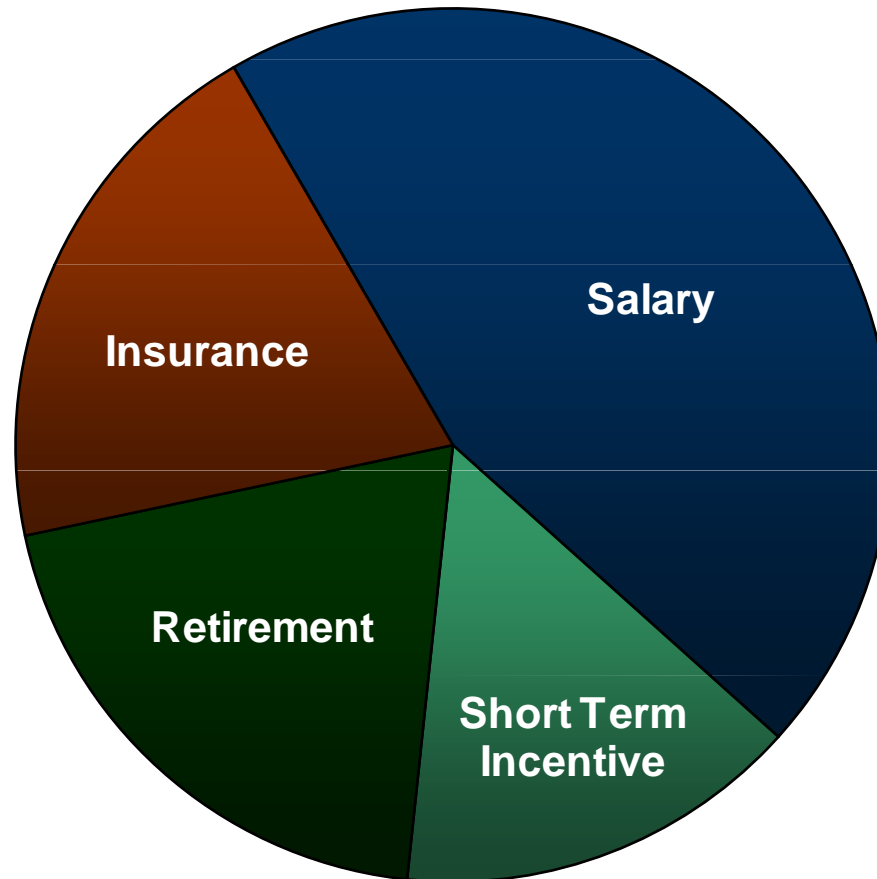
Building a Unified Financial Vision for Growing the Business

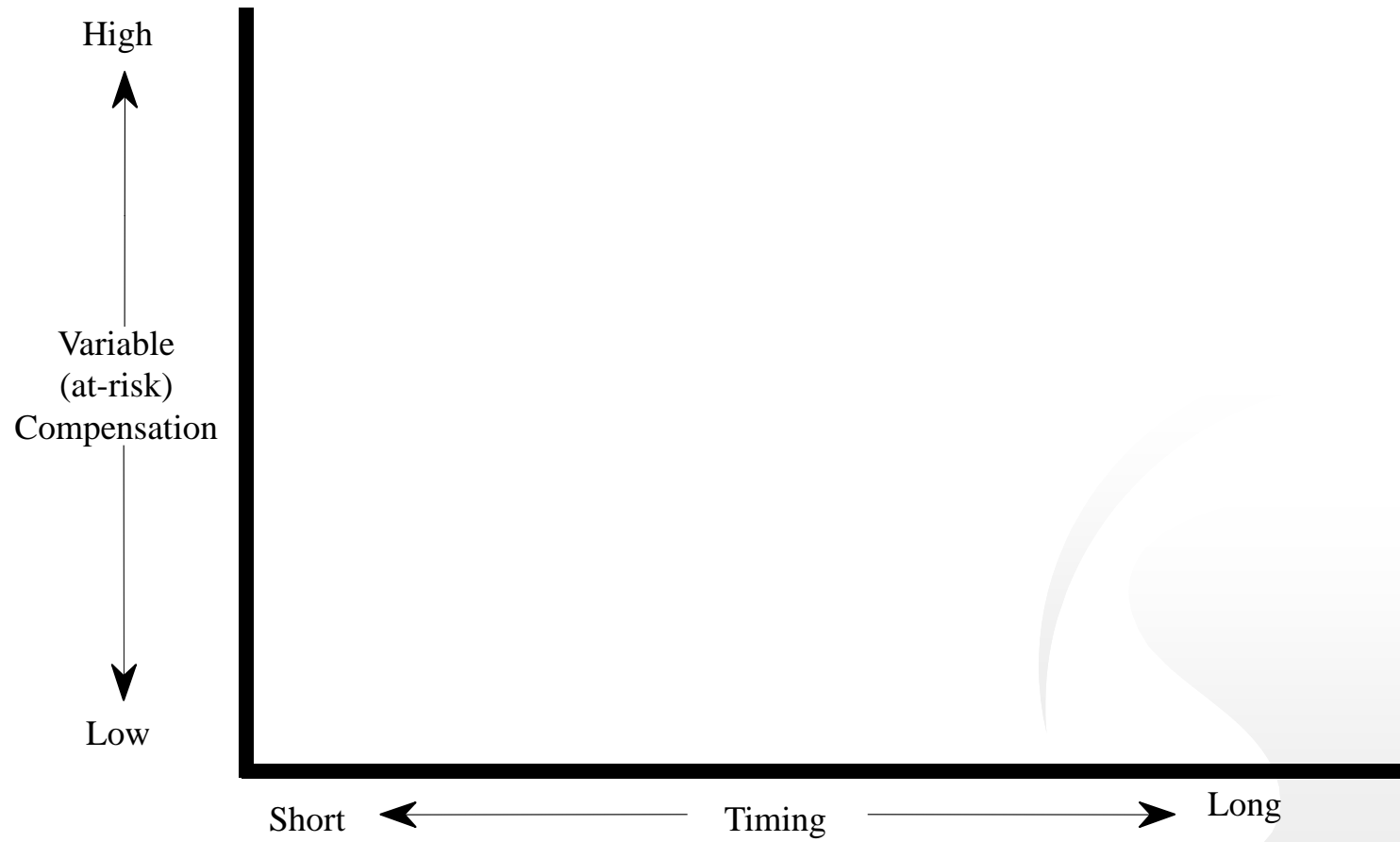


Examine Alternatives

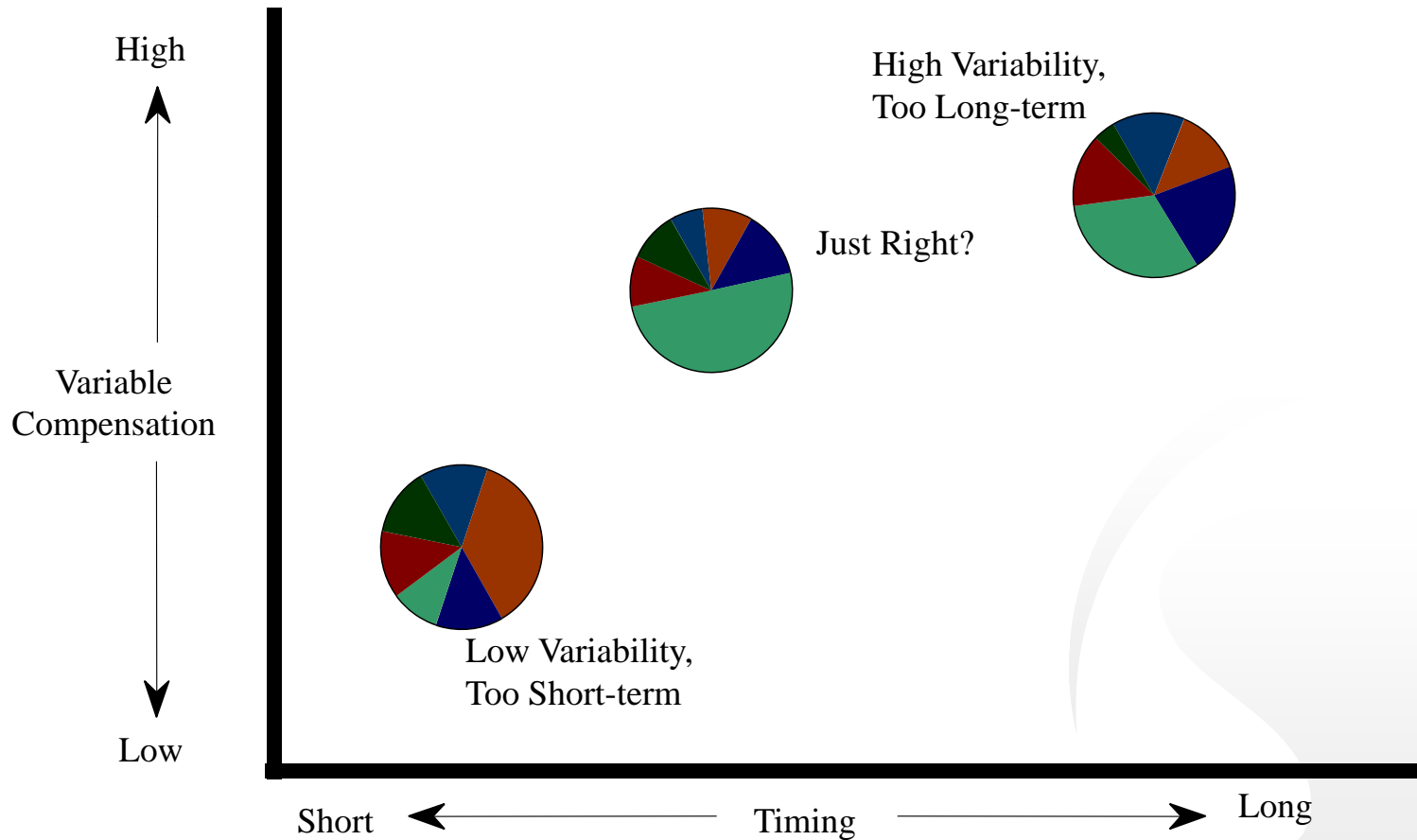


Typical Compensation Allocation

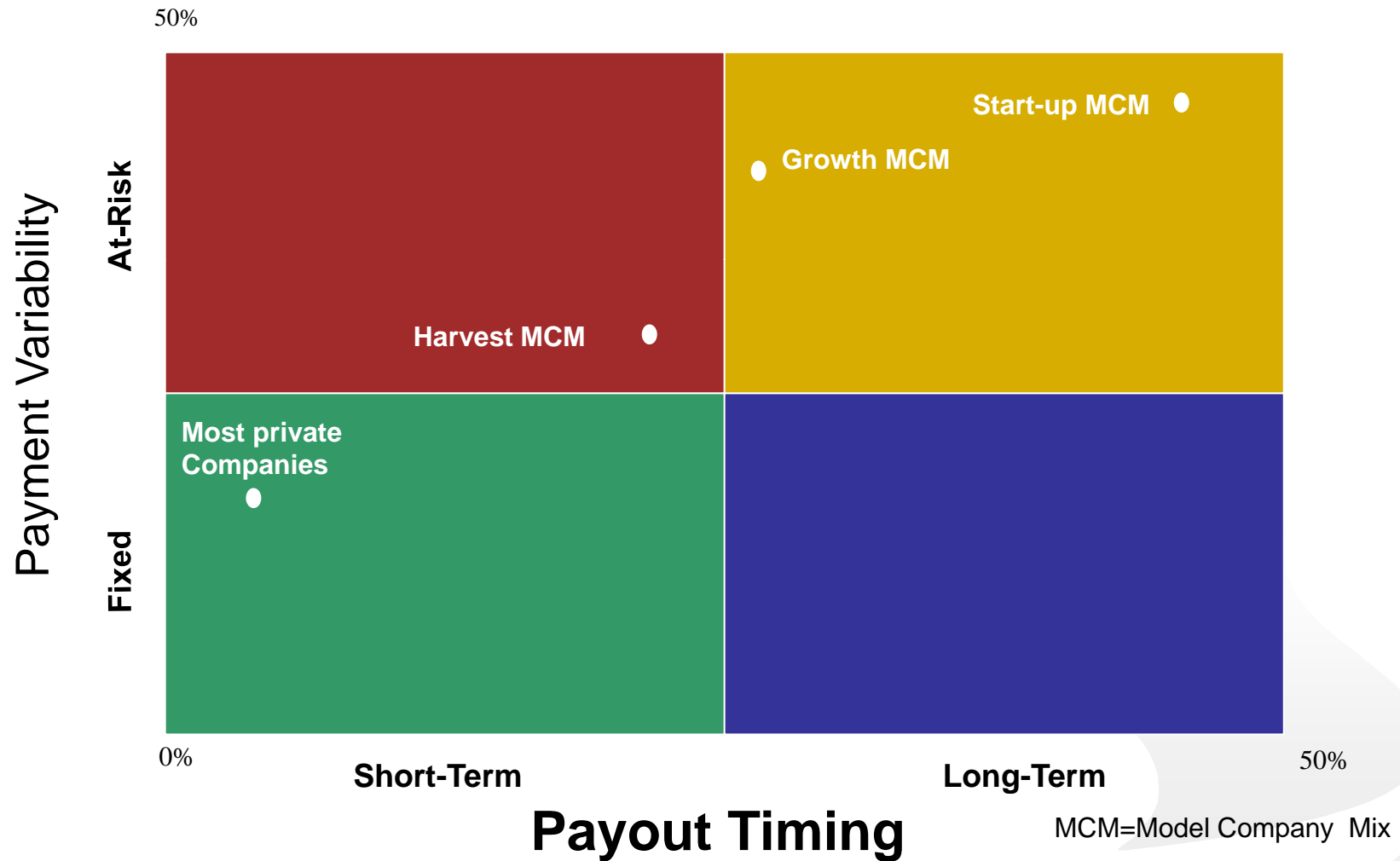




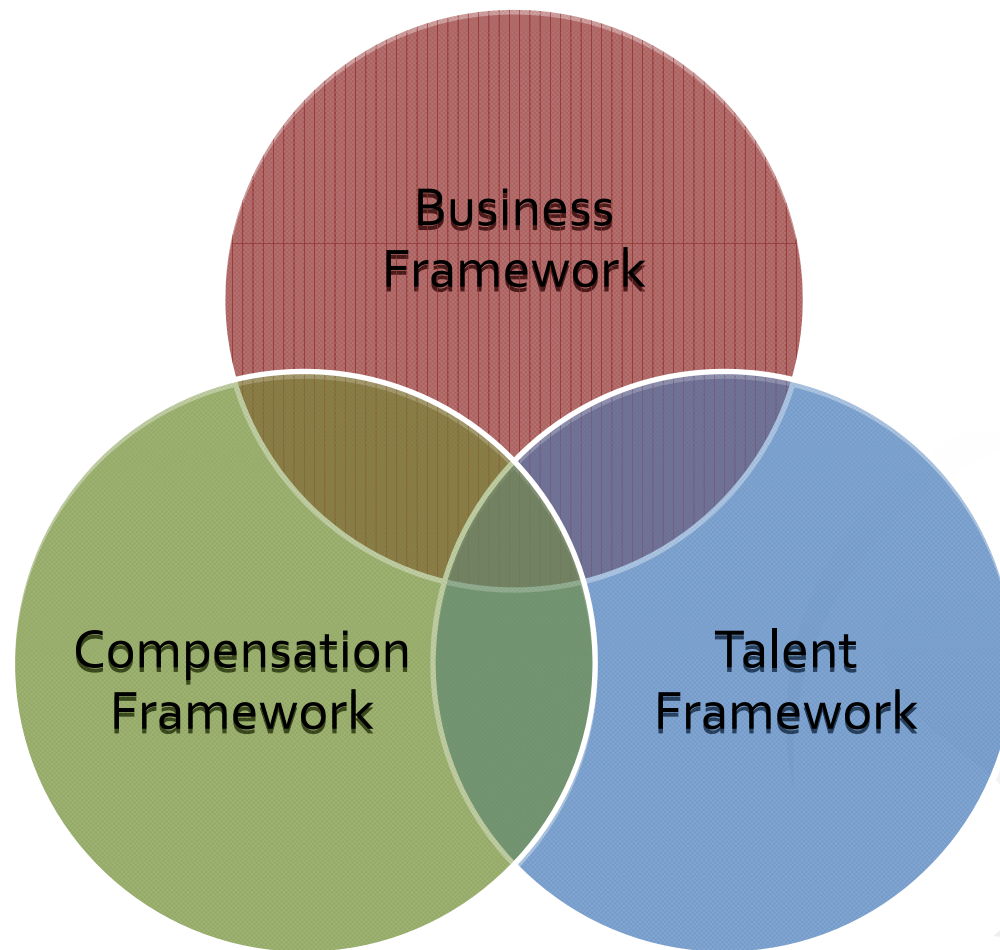
Identifying Ideal Compensation Allocations



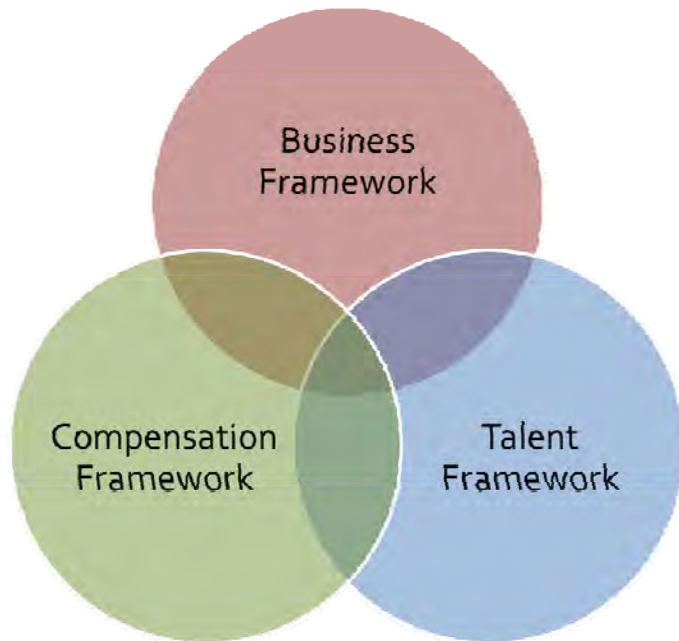
Total Compensation Positioning



Establish a Performance Framework



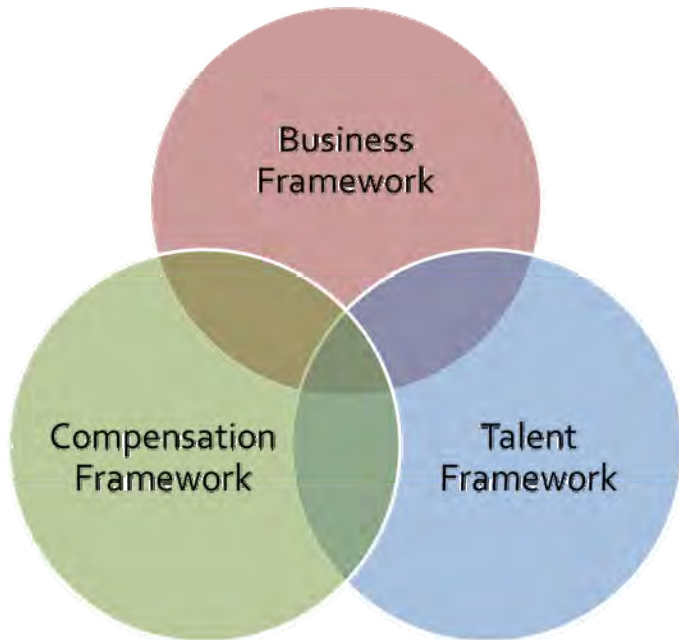
Establish a Performance Framework



Phase One—Business Framework

- Define Growth Expectations (Vision)
 - Key outcomes that must be achieved
- Define Business Model and Strategy
 - Performance Engine
 - How the company will compete
 - Where are growth opportunities?
- Identify Roles and Expectations
 - Establish Performance Criteria
 - Define "Success"

Establish a Performance Framework



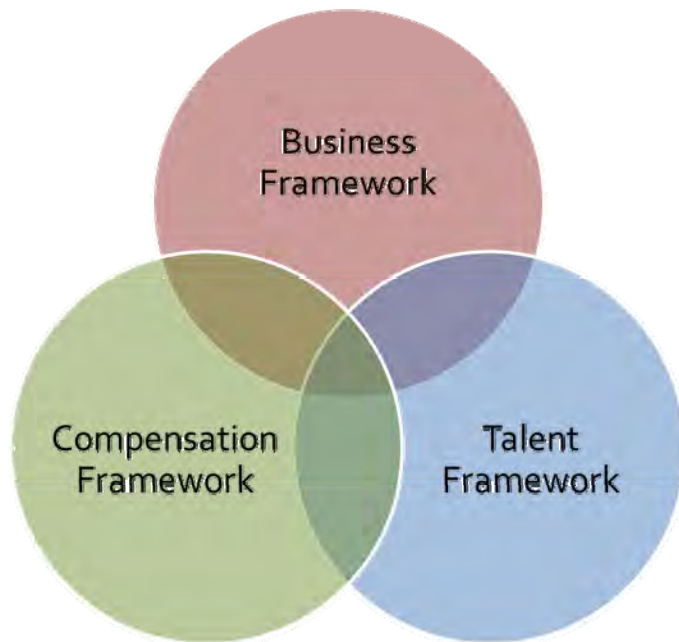
Phase Two—Compensation Framework

- Establish a pay philosophy
 - Expansive vs. Selective—or Hybrid
 - Define what the company is willing to pay for
- Engineer a pay strategy
 - Structure
 - Mindset
- Adopt a “Total Rewards” Approach

Total Rewards Approach



Establish a Performance Framework

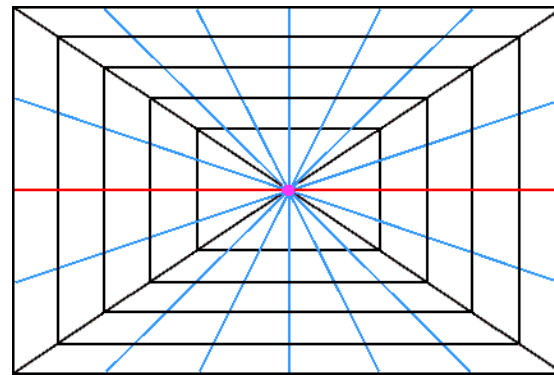


Phase Three—Talent Framework

- Identify Key Producers
 - Meeting “success” standards
- Identify Talent “Gaps”
 - Recruiting Strategy
- Communicate Expectations
 - Define success
- Communicate Rewards
 - Philosophy
 - Programs
 - Value Statement

Proper View of Compensation

- Strategic Tool
- Not One Dimensional, it's Multi-Faceted
- Define:
 - Role
 - Outcomes
 - Financial Partnership
- Communicate:
 - What's Important
 - Priorities



Form of Pay	Purpose	Standard	Investment	ROI
Salaries	Provide for the current cash needs of our executives	40-50th percentile for peer group	\$500,000	Achieve ROA standard of 0.75%
Short-term Incentives	Enhance current cash payments to executives for achieving top and bottom line annual goals	30-40% of base salary	\$168,000 (Target)	15% revenue growth and 12% margin
Long-term Incentives (Cash)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Long-term Incentives (Equity)	Retain execs; focus them on long-term earnings growth; align with shareholder interests; meet wealth accumulation needs	15-20% of base salary	\$84,000 (Target)	Long-term growth in earnings (double earnings = share 13% of new value)
Core Benefits	Meet basic security needs of the executives	50th percentile for peer group	\$25,500	ROA of 0.75%
Executive Benefits	Enhance basic security needs and meet market standards for perquisites	50th percentile for peer group	\$24,000	ROA of 0.75%
Qualified Retirement	Provide wealth accumulation opportunity for executives	40th percentile (3% of salary)	\$15,000	ROA of 0.75%
Supplemental Retirement	Strengthen rewards value proposition to help recruit and retain executives; meet wealth accumulation needs	30th percentile compared to banks that have plans	\$135,000	ROA of 0.9%

Measuring the Return on Compensation

ROTRI™

Return on Total Rewards Investment™

Measuring the return on your compensation investment



How much is the Total Rewards Investment?

- Salaries
- Commissions
- Bonuses
- Deferred award accruals (LTIP)
- Core benefits
- Executive benefits
- Retirement contributions
- Payroll taxes



What return do you get on that investment?

____%



ROTRI™ Example:

Capital Account	\$ 20,000,000
Cost of Capital	12%
Capital Charge	\$ 2,400,000
Operating Income	\$ 10,000,000
Productivity Profit	\$ 7,600,000
Total Rewards Investment	\$ 25,000,000
ROTRI™	30.4%

(ROTRI™ = Productivity Profit/Total Rewards Investment)

ROTRI™ Example:

Capital Account	\$ 20,000,000
Cost of Capital	12%
Capital Charge	\$ 2,400,000
Operating Income	\$ 10,000,000
<u>Productivity Profit</u>	<u>\$ 7,600,000</u>
Total Rewards Investment	\$ 25,000,000
ROTRI™	30.4%

Variable Pay Plans (Value Sharing) are financed from Productivity Profit

Link Company & Employee Goals

Employee "Hierarchy of Needs"

5 Wealth Accumulation

Wealth Multiplier Philosophy

4 Value Sharing

Short & Long-Term Incentive Plans

3 Retirement Planning

Qualified & Executive Retirement Plans

2 Risk Protection

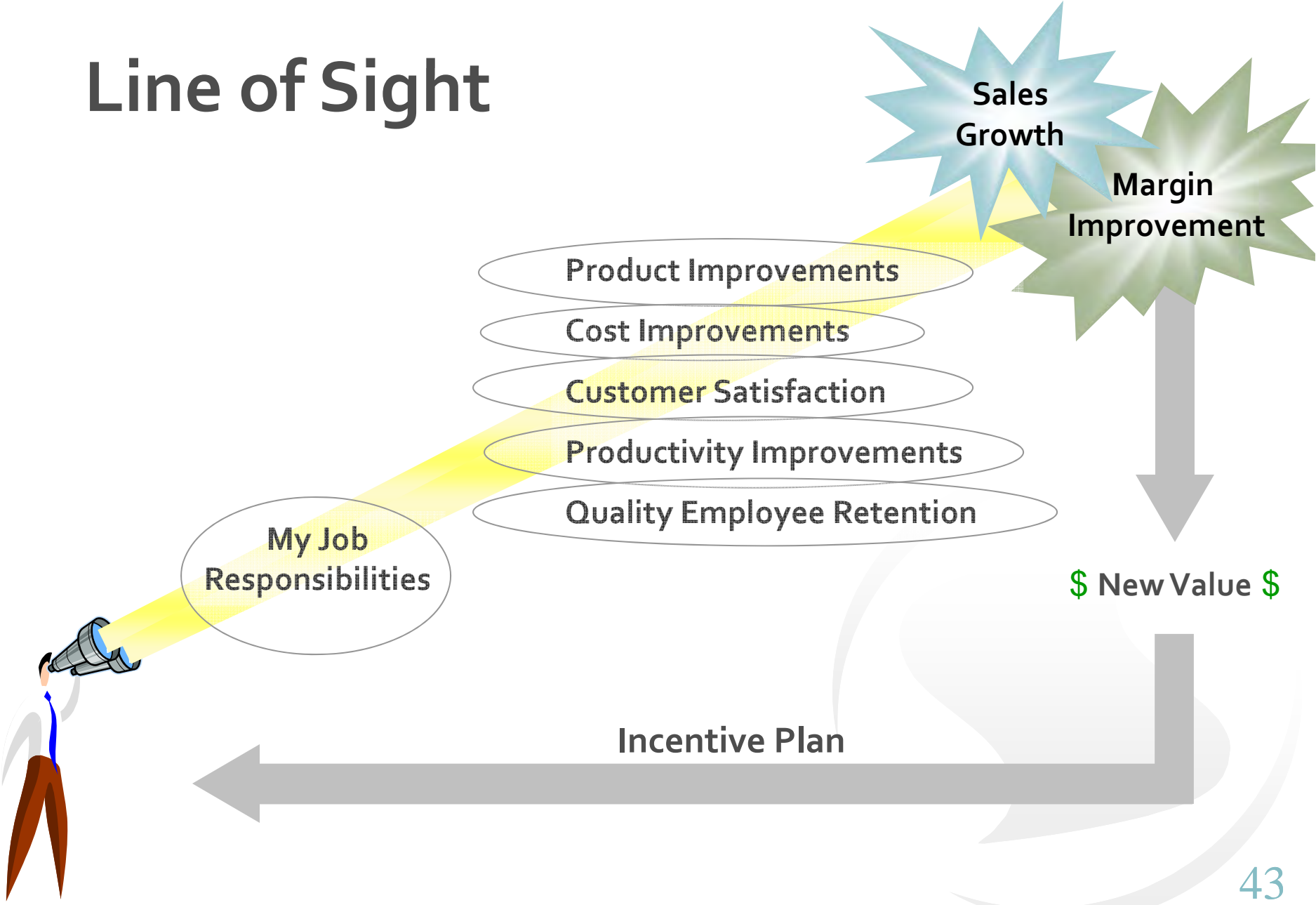
Comprehensive, Flexible Benefits Plan

1 Cash Flow & Living Standard

Salary & Bonus

Clear Pay Philosophy

Line of Sight



Rewards to Results



What makes a compensation strategy successful?

The measure should be whether or not it is fulfilling its role



Key Questions—Value Creation

- Before designing the plan, did the company clearly define value creation?
- Does the plan include metrics consistent with that definition?
- Does value sharing occur out of productivity profit?

If the answer is yes, then it means the plan is only paying out value when value has been created—it's self-financing. This also suggests that during periods of economic decline or stagnation, the plan is self-restricting in its payouts. That's a successful approach.



Key Questions—Philosophy

- Does the company have a clear philosophy statement?
- Is the pay philosophy communicated effectively to employees?
- Are the company's compensation strategies consistent with the pay philosophy?

If you answered affirmatively to each of those questions, then the company is being clear about what is willing to "pay for" and is implementing plans that follow that rule. This again must be considered a successful approach.



Key Questions—Market Pay

- Does the company compare its pay strategies to market pay standards?
- Does the philosophy statement define where the company wants to be relative to market pay?
- Is an “internal equity analysis performed?

If this is the approach being adopted, then the company is using some outside metrics to determine if it is over or underpaying for certain functions. If it likewise offers significant upside potential relative to the market, within defined value creation/sharing parameters defined in the first bullet point, then it knows it has a competitive advantage in attracting key producers. That's also a successful approach to pay.



Key Total Rewards

- Does the company market a future?
- Is there a clear & compelling vision?
- Is there a positive work environment?
- Are there opportunities for personal and professional development?
- Is the financial partnership clearly defined?

If a company adopts this framework, it is not expecting remuneration to be the sole issue upon which attracting and retaining key producers is based. If it pays attention to each of those questions, and works hard to ensure evaluation and implementation in all categories, it will become more successful at becoming a magnet for the "right talent." Hence, a total rewards approach is a successful one.





Type Your Questions

Special Offer

One hour consulting call with a VisionLink principal at no charge

(CEO or other senior leader)

Indicate interest on final survey

Next Online Seminar:

“Long-Term Incentive Plans: Which is Right for Your Company?”

To be held on:
Tuesday, September 24 , 2013

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The screenshot shows the Phantom Stock website homepage. At the top left is the logo "Phantom Stock The Equity Alternative" with a green arrow pointing up and to the right. To the right of the logo is a green navigation bar with white text: "KNOWLEDGE CENTER", "TOOLS", "BUILD A PLAN", "BLOG", "ABOUT US", and "CONTACT". In the top right corner, it says "POWERED BY VISIONLINK". Below the navigation bar is a large light gray banner. On the left side of the banner, there are three green arrow-shaped buttons pointing right, labeled "WHAT IS IT?", "WHAT WILL IT CHANGE?", and "WHERE DO I BEGIN?". To the right of these buttons, the text "A way to share ~~equity~~ Value" is displayed, with "equity" crossed out in red and "Value" written in red cursive. In the top right corner of the banner, there is a red play button icon and the text "Phantom Stock Watch overview". Below the banner is a row of four white boxes, each with a green header and an icon. The first box is titled "KNOWLEDGE CENTER" and has an information icon; its text says "Explore our wiki and find the answers to your Phantom Stock questions." The second box is titled "TOOLS" and has a briefcase icon; its text says "Decide whether Phantom Stock is a fit for your company." The third box is titled "BUILD A PLAN" and has a wrench and screwdriver icon; its text says "For 'do-it-yourselfers.' Follow this guide to create your own plan." The fourth box is titled "BLOG" and has an RSS icon; its text says "Read the latest discussions about Phantom Stock and other value sharing strategies." At the bottom of the page is a dark green footer bar with white text: "Knowledge Center Tools Build a Plan Blog About Us Contact" and "© 2012 PhantomStockOnline.com".

You can also subscribe to our blog

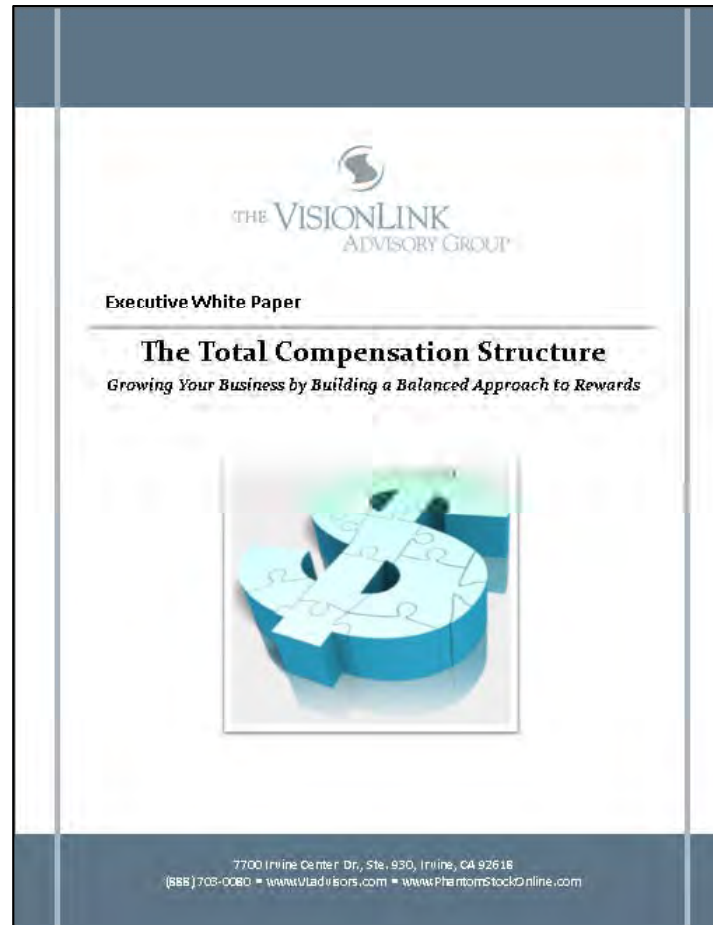
www.VLadvisors.com

The screenshot shows the homepage of The VisionLink Advisory Group. At the top left is the logo, and at the top right is a 'Client Login' button. Below the logo is the phone number (888) 703 0080. A navigation bar contains links for Home, About Us, Client Profile, Knowledge Center, Speaking Engagements, Events, Blog, and Contact Us. The main content area features a large image of a mountain peak. To the right of the image is a featured article titled 'How should I Share Value?' with a 'Learn More' button. Below the image are three smaller article teasers: 'WHAT IS PHANTOM STOCK?', 'HOW SHOULD I SHARE VALUE?', and 'HOW DO I END ENTITLEMENTS?'. The 'Events' section lists four dates with descriptions: 06/21/2012, 06/26/2012, 07/19/2012, and 07/24/2012. There is also a 'Join our webinar invitation list' form with an 'Email Address' field and a 'Go' button. At the bottom, there are three columns with titles: 'ASK THE RIGHT QUESTIONS', 'FOLLOW THE RIGHT PROCESS', and 'CHOOSE THE RIGHT COACHES', each with a brief introductory sentence.

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New White Paper



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Thank you for attending

Please complete our brief survey immediately following our presentation.

We value your input.

You may request a copy of our slides, White Paper and the 1-hour free consultation time with one of our principals.



Q&A

The VisionLink Advisory Group

Competitive Salary Services Department



Thank you!



Ken Gibson

Senior Vice President

(949) 265-5703

kgibson@vladvisors.com

Joe Miller

Senior Consultant

(949) 265-5708

jmillier@vladvisors.com

